ORIGINAL

OPEN MEETING AGENDA ITEM

0000020952

BEFORE THE ARIZONA CORPORATION COMMISSION

RECEIVED

2005 JUL -6 P 4: 48

AZ CORP COMMISSION
DOCUMENT CONTROL

Arizona Corporation Commission
DOCKETED

JUL 06 2005

DOCKETED BY

12

JEFF HATCH-MILLER, CHAIRMAN
MARC SPITZER, COMMISSIONER
WILLIAM A. MUNDELL, COMMISSIONER
MIKE GLEASON, COMMISSIONER
KRISTEN K. MAYES, COMMISSIONER

IN THE MATTER OF THE APPLICATION OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. FOR A RATE INCREASE.

DOCKET NO. E-01773A-04-0528

IN THE MATTER OF THE APPLICATION OF SOUTHWEST TRANSMISSION COOPERATIVE, INC. FOR A RATE INCREASE.

DOCKET NO. E-04100A-04-0527

EXCEPTIONS OF INTERVENOR MOHAVE ELECTRIC COOPERATIVE TO RECOMMENDED OPINION AND ORDER FOR AEPCO

Mohave Electric Cooperative, Inc. ("Mohave"), by and through its attorneys undersigned, respectfully files these exceptions pursuant to A.C.C. R.14-301(b) to the Recommended Opinion and Order concerning the Arizona Electric Power Cooperative, Inc. ("AEPCO") in the above captioned matter.

A. MOHAVE'S EXCEPTIONS - SUMMARIES

1. When examining appropriate equity levels the Recommended Opinion and Order and the Staff fail to distinguish between the appropriate goals and objectives of a generation and transmission cooperative and a distribution cooperative when examining equity.

2. In requiring a three (3) step increase, the Commission is setting rates for the future which is unprecedented and adversely impacts end use customers and may be unnecessary.

3. By not allowing its Board of Directors, elected by its members who have responsibility to the ratepayers, to make the decisions on when and whether to ask customers to pay increased rates in the future, the Recommended Opinion and Order fails to take into account the governance provisions of Arizona Electric Power Cooperative ("AEPCO").

4. Without factual filed data to review, there must be an ACC proceeding to determine whether or not the rate increases proposed for the future are to be implemented.

5. Concerning Anza cost studies, Staff does not sufficiently understand the distinction between operation of a multi-state distribution cooperative (like Garkane and Columbus which operate and serve at retail in two (2) states), and a G&T cooperative like AEPCO serving at wholesale (and indeed making sales, perhaps, in many states). All of the Staff examples concerning the issue of Anza Electric Cooperative were examples of retail distribution cooperatives. The focus, if any at all, should be on the transmission rate.

B. REASONING

1. When examining appropriate equity levels the Recommended Opinion and Order and the Staff fail to distinguish between the appropriate goals and objectives of a generation and transmission cooperative and a distribution cooperative when examining equity.

a. When examining equity, the Recommended Opinion and Order and the Staff fail to distinguish between appropriate equity requirements of a generation and transmission cooperative and distribution cooperative. As a result, they improperly emphasize increasing equity and rates to the harm of members and end users. A G&T thirty percent (30%) equity goal is a lead weight and an economic travesty to foist upon the backs of ratepayers when the actual lenders do not require it. In this case, the lender does not expect equity in AEPCO to be thirty percent (30%) or even on a track to thirty percent (30%). The Cooperative Finance Corporation ("CFC") representative testified that CFC supported the original filing of AEPCO. the only purpose of a high equity ratio is to permit greater return of patronage capital.

The lender looks to the "take and pay" provisions of the All Requirements Contract and the Partial Requirements Contract for its ultimate security. Even with less than thirty percent (30%) equity RUS will permit return of patronage capital. Therefore, availability to AEPCO of funds by way of RUS/CFC borrowing is actually dependent on the strength of its members, the credit worthiness of the All Requirements Members and Partial Requirements Members. Certainly the TIER and DSC are the additional important criteria which determine whether or not new loans will be made. It is correctly pointed out that there is no "risk factor" (attributed to low equity or low TIER or DSC) assigned to the RUS/CFC loans to AEPCO and, therefore, imagined "financial risk" does not increase the loan or interest expense to AEPCO because of certain ratios being achieved or not being achieved.

b. The purpose for creating a G&T is to have the least possible G&T equity so that there can be the lowest possible distribution cooperative rates, but still borrow from RUS/CFC. The G&T finances are then supported by the credit worthiness of the distribution cooperatives which are attempting to make the lowest cost rates available to the rate payer/end user, and rates acceptable to the lender. In this case CFC agreed with the filing. No G&T has an equity at the thirty percent (30%) level. When it is first created, no RUS financed G&T has any equity at all. Lenders recognize it is the economic and financial strength of G&T distribution cooperative members and ability to repay debt which determines whether or not G&T loans will be made. Not equity.

c. Distribution entities require differing levels of equity depending upon their growth and their other economic circumstances. This is the reason why a thirty percent (30%) equity is some times believed to be the appropriate target equity for a distribution cooperative. And, often, not. In the past, a high G&T or distribution equity (30%) has resulted in attempts by investor-owned utilities using in effect the members' own money to take over rural electric cooperatives and to take over the territories and to change the governance and manner by which distribution rates are set.

d. Mohave Electric Cooperative is (and Sulphur Springs Electric Cooperative soon will be) a Partial Requirements AEPCO member. In the future, AEPCO will not have resource responsibility or planning responsibility for sixty-five percent (65%) of what now constitutes its current load (which 65% load responsibility will continue to be paid and assumed by Mohave and Sulphur Springs. Today, AEPCO is not responsible for Mohave's future planning or resource needs. Mohave is 35.8% of AEPCO's current load and is obligated to pay. These facts are important when considering target equity growth for AEPCO and the impact of increasing rates on Partial Requirements customers. The impact of an equity factor on a Partial Requirements member may be unfair when the G&T has no planning or resource responsibility and Mohave has no obligation to AEPCO equity except to pay 35.8% of the existing AEPCO debts, operating and maintenance expenses, and 35.8% of the future expenses of "running" AEPCO (not building).

e. The use of Golden Spread as a model was outrageous in this case. Mr. Ramirez from Staff admitted on the stand that he simply received from the Fitch Company an analysis of Golden Spread which was a G&T, that he had never done a G&T case, and he made no separate inquiry as to the nature of the operations and the organization of Golden Spread. Mr. Ramirez did not even submit the complete article on Golden Spread (while cross examination was brief, it should be noted that Golden Spread was revealed to be represented by the same consulting firm ("Guernsey") as represents Mohave Electric Cooperative and Sulphur Springs Electric Cooperative and Trico Electric Cooperative). The Golden Spread operation is unique. It does not borrow from CFC or RUS. It finances on the market (Mr. Minson testified that AEPCO would never go to the market because the available funds from RUS and CFC were at a much more attractive rate and, therefore, would not need market equity ratios). The size, the complexity and the needs of Golden Spread make it not a typical G&T and, therefore, the reference by Mr. Ramirez to the ratios and the performance of Golden Spread as a measure for AEPCO to achieve was totally inappropriate.

f. No one with experience has indicated that a G&T equity of thirty percent (30%) is an appropriate goal. Mohave concurs in the Opinion to the extent that the Opinion points out that while equity is being built, thirty percent (30%) is not a goal that needs to be evaluated at this time.

g. In the future AEPCO should be allowed by Staff to use the calculations of TIER and DSC in the manner and using the methodology that the lenders use because it is the lenders which are the ultimate providers of the borrowed funds (the "money"). Those compilations of statistics adopted by RUS and CFC meet all of the lender's requirements; and, if they are sufficient for the lenders, and if they result in less upward rate pressure on the end users, and if they are reliable, then they should be satisfactory to Staff. The goal is to keep rates low, and AEPCO eligible to borrow from RUS and CFC.

2. In requiring a three (3) step increase, the Commission is setting rates for the future which is unprecedented and adversely impacts end use customers and may be unnecessary.

a. The step rate imposition without a hearing or a filing on the data showing its need with opportunity to intervene and to comment is not consistent with fairness to either the members such as Mohave or the end use customers. Such action is not good regulatory process. It was prompted by Ramirez's threat to not approve a loan, already approved by CFC/RUS, unless rates were higher.

b. A future step rate increase should be granted only on the basis of demonstrated need at the time and based on the advice of lenders and an analysis of current ratios and current circumstances (Mohave does not suggest that a full rate case is required, only that there needs to be an opportunity to be heard and to examine data before action is taken).

c. The CFC lender supported the original Application of AEPCO. This should be a signal to the Commission and to the Staff that when the banker is willing to lend the money based on the data and on the projections derived from that data, it takes some very serious analysis and reasoning and some serious circumstances to jump in three (3) steps out into the future and propose rate increases which the lender did not require. The Commission should be as sensitive to end use customers as the lenders have been.

d. There was insufficient time for analysis and insufficient opportunity to examine the three (3) step data proposal. Mention is made of this in the transcript. All of this is a reason why the step rate imposition should not occur without a filing of data and an opportunity to be heard and a hearing on the data.

e. Since when does Staff have authority to threaten a utility that while a rate will be approved, a pending loan will not even though the lender approved the loan? What is the role of the Commissioners?

3. By not allowing its Board of Directors, elected by its members who have responsibility to the ratepayers, to make the decisions on when and whether to ask customers to pay increased rates in the future, the Recommended Opinion and Order fails to take into account the governance provisions of Arizona Electric Power Cooperative ("AEPCO").

a. It is insulting to the Directors of AEPCO to deny them their rightful role as policy making managers and representatives of member-owner rate payers to demand prior presentation and approval by it of future data and future statistics upon which future rate increases by the ACC will be based. This is what is being proposed by Staff. It is upside down rate making.

b. Cooperatives are the only democratic one-man one-vote public service corporation utilities governed by the Arizona Corporation Commission with rate stability for over 200,000 people. For twelve (12) years AEPCO, through its Board, has been able to manage its affairs through its Board of Directors with the support of its members and has not required a rate increase. This is an admirable twelve (12) year achievement. Where is the G&T expertise that now overrides this management?

c. Approximately 200,000 end use customers have benefited from twelve (12) years of the AEPCO Board decisions on stabilizing rates and delay of requests for rate increases. The Commission Staff should not be substituting its opinions in a manner which causes unneeded increased adverse rate impacts on customers.

d. The members which comprise the ownership of AEPCO are consulted on rates in the rate making process, and each member of the Board of Directors considers (as well as the AEPCO Board) the impact of rates on members before a rate case is even filed.

e. Lenders are consulted before requests for rate increases are filed.

f. It is, therefore, wholly inappropriate to refer to the Board of Directors of AEPCO as an entity with an interest adverse to that of the AEPCO corporate body by saying that the duly elected and fiduciarily responsible AEPCO Board members could "block" rate increases or take actions which would disadvantage "AEPCO" in violation of their fiduciary duty. After all, who is AEPCO? It is the sum of the very members represented by the Board of Directors who have only one (1) significant overriding goal: to assure AEPCO continues as an economically viable and successful G&T entity, providing "member-owner" service <u>at the lowest possible rates</u>. If before step rates are implemented the Board of Directors of AEPCO cannot be heard and have a "say" on the step rate increases, what kind of a signal is it that the Commission intends to send to a democratically run organization such as a cooperative? Who does the Staff think is protecting? The lender? No. The members? No. The end use customer? From what?

4. Without factual filed data to review, there must be an ACC proceeding to determine whether or not the rate increases proposed for the future are to be implemented.

a. As proposed in this three (3) step process. without a hearing, members and ratepayers are denied an opportunity to participate and this is a fundamentally unfair situation. AEPCO never agreed to the step increases, except in the form of a resolution.

b. Future events are uncertain, and an increase may be unnecessary in 2005, 2006 and 2007; and, if it is unnecessary, there is no purpose for a step increase simply to accelerate some myth about growing a thirty percent (30%) equity (a myth based on a misunderstanding of the role of equity in a G&T).

c. As noted above, the lenders originally approved the AEPCO rate filing as originally filed (and the pending loan).

d. It is unfair to Partial Requirements members to increase rates without a hearing since Partial Requirements member obligations are fixed. The Partial Requirements member pays its proportionate share of the debt. Since the Partial Requirements member pays its proportionate share of the debt and any future agreed upon joint ventures; and since the lenders rely on the credit worthiness of the Partial Requirement member and the All Requirements members and not the equity of AEPCO; and since as long as the debt is paid the Partial Requirements members are owed no duty by AEPCO for planning or for resources, the Partial Requirements member is punished by the Staff equity proposal. All of the foregoing are arguments in support of having a hearing before the imposition of a rate increase.

5. Concerning Anza cost studies, Staff does not sufficiently understand the distinction between operation of a multi-state distribution cooperative (like Garkane and Columbus which operate and serve at retail in two (2) states), and a G&T cooperative like AEPCO

serving at wholesale (and indeed making sales, perhaps, in many states). All of the Staff examples concerning the issue of Anza Electric Cooperative were examples of retail distribution cooperatives. The focus, if any at all, should be on the transmission rate.

a. All members of a G&T are treated the same since all assume their share of the *same* costs and have the same rates.

b. There are no retail meters, customer service or administration expenses, or distribution expenses for the G&T to account for when serving Anza. The only cost is the wholesale cost of power and transmission, which is another case for Southwest Transmission Cooperative.

c. Garkane and Columbus as distribution cooperatives serving at retail have man hours to account for and allocate, supplies and offices and physical equipment on the ground, all of which needs to be accounted for as it is spread out over two (2) states. A G&T simply sells a common commodity at wholesale under rates which recover its cost of wholesale service and are approved by the governing Board and hence, by the members.

d. The Anza Electric Cooperative issue is a non-issue. In the future if the AEPCO requests a waiver, it should be granted or the matter addressed in a transmission case.

C. SUMMARY

1. There should be no step increases without a filing and a hearing.

2. Partial Requirements members should not be punished by rates designed to achieve an equity level based on myth.

3. The equity plan should be accomplished by a seminar from RUS and CFC on who they are, why they lend, how they lend, what criteria they demand, what criteria they waive, how they assess a loan and what is the proper role of equity in a G&T with All Requirements Members and Partial Requirements Members.

RESPECTFULLY SUBMITED this 6th day of July, 2005.

CURTIS, GOODWIN, SULLIVAN,
UDALL & SCHWAB, P.L.C.

By: ______________________

Michael A. Curtis
William P. Sullivan
2712 North 7th Street
Phoenix, Arizona 85006-1090
Attorneys for Mohave Electric Cooperative, Inc.

PROOF OF AND CERTIFICATE OF MAILING

I hereby certify that on this 6th day of July, 2005, I caused the foregoing document to be served on the Arizona Corporation Commission by delivering the original and fifteen (15) copies of the above to:

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Copies of the foregoing were mailed this 6th day of July, 2005 to:

Michael M. Grant, Esq.
Todd C. Wiley, Esq.
Gallagher & Kennedy
2575 East Camelback Road
11th Floor
Phoenix, AZ 85016

Christopher Hitchcock, Esq.
Law Offices of Christopher Hitchcock, PLC
P.O. Box AT
Bisbee, Arizona 85603-0115
Attorneys for SSVEC

John T. Leonetti
HC 70 Box 4003
Sahuarita, Arizona 85629

Chris Kempley, Chief Counsel
LEGAL DIVISION
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ernest Johnson, Director
UTILITIES DIVISION
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

____